

CHAPTER 81-03-01.1 GENERAL CONSIDERATIONS

Section	
81-03-01.1-01	Reaudit and Reassessment [Repealed]
81-03-01.1-02	Taxpayer May Be Required to File a Pro Forma Federal Income Tax Return
81-03-01.1-03	Interest on Obligations of the United States and of the States and Their Political Subdivisions
81-03-01.1-04	Computation of Interest on Refunds [Repealed]
81-03-01.1-05	Computation of Interest on an Extension, a Late Payment, Underpayment, and Additional Tax Found Due Through Audit or Mathematical Verification [Repealed]
81-03-01.1-06	Income Tax Exemption for New and Expanding Business
81-03-01.1-07	Venture Capital Corporation
81-03-01.1-08	Tax Credits
81-03-01.1-09	Requirement to Report Federal Changes
81-03-01.1-10	Employers Required to File Information Returns

81-03-01.1-01. Reaudit and reassessment. Repealed effective May 1, 1991.

81-03-01.1-02. Taxpayer may be required to file a pro forma federal income tax return.

1. A taxpayer who does not have a federal income tax filing requirement but who has income taxable in this state and is, therefore, required to file a North Dakota income tax return, must prepare a pro forma federal income tax or information return to determine a starting point for the North Dakota tax return. The pro forma federal income tax or information return must be filed with the state tax commissioner together with the taxpayer's North Dakota income tax return.
2. "Pro forma federal income tax return" for purposes of this article and North Dakota Century Code chapter 57-38 means a federal income tax return prepared in accordance with the provisions of the Internal Revenue Code of 1954 as amended and effective during the period covered in the tax return. The tax return must contain complete and accurate information on the taxpayer's income and deductions and must be prepared as though the taxpayer were required to file it with the internal revenue service.

History: Effective July 1, 1985.

General Authority: NDCC 57-38-56

Law Implemented: NDCC 57-38-30.3, 57-38-31, 57-38-32, 57-38-34, 57-38-42

81-03-01.1-03. Interest on obligations of the United States and of the states and their political subdivisions. Interest received from obligations of the

United States or of its possessions and from this state or its political subdivisions is not subject to income tax imposed by this state.

Interest received from obligations of any other state or its political subdivisions is subject to income tax imposed by this state for a taxpayer who files an individual income tax return form ND-2 or form 37, but is not subject to income tax imposed by this state for a taxpayer who files an individual income tax return form ND-1 or form 37-S.

"Obligations" as used in this section means only those obligations, such as municipal or other government bonds, arising out of the borrowing power of the federal government or a state government or its political subdivisions.

History: Effective July 1, 1985; amended effective June 1, 2002.

General Authority: NDCC 57-38-56

Law Implemented: NDCC 57-38-01.2, 57-38-01.3, 57-38-30.3

81-03-01.1-04. Computation of interest on refunds. Repealed effective March 1, 1990.

81-03-01.1-05. Computation of interest on an extension, a late payment, underpayment, and additional tax found due through audit or mathematical verification. Repealed effective September 1, 1997.

81-03-01.1-06. Income tax exemption for new and expanding business.

1. When a taxpayer is granted an exemption from income tax pursuant to North Dakota Century Code chapter 40-57.1, the exemption must be prorated, when necessary, in the first and last years in order to exempt income for a period not to exceed sixty months.
2. The amount of the yearly income tax exemption for new and expanding business is limited to income earned from the new business or expansion in each tax year reduced by the amount of federal tax assignable to the North Dakota exempt income which was included in federal taxable income.
3. When the project operator is a partnership, S corporation, or limited liability company, the income tax exemption flows through to the partners, shareholders, and members.
4. The conditions for reapplication set forth in North Dakota Century Code chapter 40-57.1 apply to the income tax exemption. A project operator must reapply for the income tax exemption if these conditions are met.
5. The office of the state tax commissioner must be notified of any changes in ownership of a new industry which has been granted an income tax exemption. A change of ownership includes transfer of a partnership

interest, a stock interest in a subchapter S corporation, or a membership in a limited liability company.

6. The income tax exemption may not be claimed by an individual taxpayer on individual income tax form ND-1 or form 37-S.
7. A taxpayer with both exempt and nonexempt activities shall prorate its income pursuant to the provisions of North Dakota Century Code chapter 57-38.1.
 - a. If the taxpayer has only North Dakota activity, exempt income must be determined by multiplying income from all activities, exempt and nonexempt, by a fraction, the numerator of which is the sum of its exempt property, sales, and payroll factors and the denominator of which is three.

EXAMPLE:

Facts:	Exempt Plant	Other North Dakota Activity	Total North Dakota Activity
Property	\$5,000,000	\$10,000,000	\$15,000,000
Payroll	\$750,000	\$1,000,000	\$1,750,000
Sales	\$20,000,000	\$35,000,000	\$55,000,000
Apportionable income	\$50,000,000		
Federal tax liability	\$17,500,000		

Determine North Dakota exempt income:

- (1) Compute apportionment factor of exempt activities.

Property factor =	$\$5,000,000 / \$15,000,000 =$.333333
Payroll factor =	$\$750,000 / \$1,750,000 =$.428571
Sales factor =	$\$20,000,000 / \$55,000,000 =$	<u>.363636</u>
	$1.125540 / 3 =$.375180

- (2) Compute exempt income.

Apportionable income	\$50,000,000
Federal tax liability	<u>\$17,500,000</u>
North Dakota income after federal tax deduction	\$32,500,000

Apportionment factor of exempt activities	<u>.375180</u>
Exempt income	\$12,193,350

- b. If the taxpayer has multistate business activity, North Dakota income must first be determined by including all exempt and nonexempt activity in apportionable income and in the apportionment factor. North Dakota exempt income is then determined as in subdivision a.

EXAMPLE:

Multistate corporation

Facts: Utilize the same facts in the prior example, and add:

Total activity within and without North Dakota

Property \$100,000,000

Payroll \$5,000,000

Sales \$200,000,000

Determine North Dakota exempt income:

- (1) Compute the North Dakota apportionment factor, including tax-exempt activity.

$$\begin{array}{rcl}
 \text{Property factor} & \$15,000,000/ & \\
 = & \$100,000,000 = & .150000 \\
 \text{Payroll factor} = & \$1,750,000/ & \\
 & \$5,000,000 = & .350000 \\
 \text{Sales factor} = & \$55,000,000/ & \\
 & \$200,000,000 = & \underline{.275000} \\
 & .775000/3 & .258333 \\
 & = &
 \end{array}$$

- (2) Compute the apportionment factor of the North Dakota exempt activities. For this example, the computation would be the same as that in paragraph 1 of subdivision a and would yield a factor of .375180.

- (3) Compute exempt income.

Apportionable income	\$50,000,000
North Dakota apportionment factor	<u>.258333</u>
Income apportioned to North Dakota before federal tax deduction	\$12,916,650
Federal tax liability	\$17,500,000

North Dakota apportionment factor	<u>.258333</u>
Federal tax deduction	\$4,520,827
North Dakota income after federal tax deduction	\$8,395,823
Apportionment factor of exempt activities	<u>.375180</u>
Exempt income	\$3,149,945

- c. When a partial exemption on a project or plant has been granted, the percentage of the project's nonexempt property, payroll, and sales would be added to the other North Dakota taxable activity's factors. For instance, a twenty percent exemption would mean eighty percent of the project's property, payroll, and sales would be added to the other North Dakota factors creating a taxable activity.
- d. When a company has only one operating facility which has been granted a partial exemption, North Dakota taxable income shall be computed based on total income of the operation, and a percentage of the income which is equal to the percentage of the exemption shall be deducted from the total.

History: Effective March 1, 1990; amended effective June 1, 1992; August 1, 1994; April 1, 1995; July 1, 1998; June 1, 2002.

General Authority: NDCC 57-38-56

Law Implemented: NDCC 40-57.1

81-03-01.1-07. Venture capital corporation. An individual, estate, trust, or corporation that has purchased stock in a venture capital corporation may not sell any or all of the stock back to the venture capital corporation and then purchase new stock in the same venture capital corporation to qualify for the income tax deduction and the tax credits provided for in North Dakota Century Code chapter 10-30.1.

History: Effective March 1, 1990.

General Authority: NDCC 57-38-56

Law Implemented: NDCC 10-30.1

81-03-01.1-08. Tax credits. Tax credits must be taken in the following order:

1. Tax credits with no carryback or carryforward provisions.
2. Tax credits with carryback provisions.
3. Tax credits with carryforward provisions.

If there is more than one tax credit having the same priority, the tax credits must be allowed in the order that is most beneficial to the taxpayer.

History: Effective May 1, 1991.

General Authority: NDCC 57-38-56

Law Implemented: NDCC 57-38-01.8, 57-38-01.16, 57-38-01.17, 57-38-30.1, 57-38-30.4, 57-38-30.5, 57-38.1-07

81-03-01.1-09. Requirement to report federal changes.

1. The following provisions are applicable for purposes of interpreting subsection 1 of North Dakota Century Code section 57-38-34.4:
 - a. If a change or correction to federal taxable income or federal income tax liability is initiated by the United States internal revenue service, the change or correction must be reported to the commissioner even if it does not result in an underpayment or an overpayment of federal income tax.
 - b. "Final determination" means a decision, action, or date from which no further action is taken by the taxpayer or the United States internal revenue service to resolve any dispute relating to the change or correction which was made to the taxpayer's federal taxable income or federal income tax liability. A final determination has occurred if any of the following circumstances apply:
 - (1) A taxpayer receives a notice or other correspondence from the United States internal revenue service which makes an adjustment to the taxpayer's federal taxable income based on:
 - (a) A mathematical or clerical error.
 - (b) Any other change or correction if the taxpayer has paid or arranged to pay the underpayment of federal income tax, or if the United States internal revenue service has credited or refunded to the taxpayer an overpayment of federal income tax. A final determination does not occur, however, if a taxpayer pays the tax and then files a claim for credit or refund with the United States internal revenue service.
 - (2) A taxpayer waives the restrictions on assessment and collection of all or any part of an underpayment of federal income tax by signing a federal form 870 or any other form prescribed for this purpose by the United States internal revenue service. A final determination does not occur with respect to any part of the underpayment which is not covered by the waiver. If the signature of an authorized representative

of the United States internal revenue service is required to execute this waiver, the date of final determination is when the taxpayer receives notice of the signing. A final determination does not occur, however, if a taxpayer pays the tax and then files a claim for credit or refund with the United States internal revenue service.

- (3) A taxpayer receives a federal statutory notice of deficiency and does not timely file a petition with the United States tax court for redetermination of the assessed underpayment of federal income tax. The date of final determination is when the time period within which to file the petition expires. A final determination does not occur, however, if a taxpayer pays the tax and then files a claim for credit or refund with the United States internal revenue service.
- (4) A closing agreement is executed pursuant to United States Internal Revenue Code section 7121 [26 U.S.C. 7121]. The date of final determination is when the taxpayer receives notice of the signing of the closing agreement by an authorized representative of the United States commissioner of internal revenue.
- (5) A federal court of law issues a decision which is not appealed or is not subject to appeal.
- (6) A federal court of law approves a voluntary agreement stipulating final disposition of a case.
- (7) If a taxpayer files a claim for credit or refund of all or any part of an underpayment of federal income tax, as described in paragraph 1, 2, or 3, a final determination has occurred if any of the following circumstances apply:
 - (a) The taxpayer receives notice of the disallowance of the claim for credit or refund from the United States internal revenue service and the taxpayer does not appeal the disallowance or file a suit for refund.
 - (b) The taxpayer receives notice of the allowance of the claim for credit or refund from the United States internal revenue service.
 - (c) Receipt of the refund from the United States internal revenue service, if no prior notice is received.
 - (d) The provisions of paragraph 4, 5, or 6 apply.

2. The following provisions are applicable for purposes of interpreting subsection 2 of North Dakota Century Code section 57-38-34.4:
 - a. If a taxpayer initiates the filing of the amended federal income tax return, the taxpayer must also file an amended state income tax return even if it does not result in payment of additional tax.
 - b. To request a credit or refund of tax, a taxpayer must file an amended state income tax return either within the time period prescribed in subsection 1 of North Dakota Century Code section 57-38-40 or within the ninety-day time period prescribed in subsection 2 of North Dakota Century Code section 57-38-34.4.
3.
 - a. A change or correction to federal taxable income or federal income tax liability must be reported on an amended state income tax return except as provided in subdivision b.
 - b. An alternative report may be elected to report an increase in North Dakota tax liability as a result of a change or correction to federal taxable income or federal income tax liability. The alternative report must contain the following:
 - (1) A statement that the information is submitted in lieu of an amended return pursuant to subdivision b of subsection 3 of section 81-03-01.1-09.
 - (2) A description of the change or correction to federal taxable income or federal tax liability and the effect which the change or correction has on the statutory adjustments provided for in North Dakota Century Code sections 57-38-01.2 and 57-38-01.3.
 - (3) An allocation or apportionment of the change to North Dakota tax liability and a computation of the adjusted North Dakota tax liability.

This alternative report is subject to audit and assessment as if it were an amended return.

- c. When reporting a change or correction to federal taxable income or federal income tax liability pursuant to subsection 1 of North Dakota Century Code section 57-38-34.4, a taxpayer must also submit the following items:
 - (1) A copy of the applicable federal waivers.
 - (2) A copy of the documentation evidencing that a final determination has been made with respect to the federal change or correction.

4. A change or correction to federal taxable income or federal income tax liability that affects a year other than the year in which the change or correction occurs must also be reported in accordance with subsection 3.

History: Effective November 1, 1991; amended effective November 1, 1992; June 1, 2002.

General Authority: NDCC 57-38-56

Law Implemented: NDCC 57-38-34.4

81-03-01.1-10. Employers required to file information returns.

Employers are subject to subsection 1 of North Dakota Century Code section 57-38-42 except with respect to the payment of wages to an employee.

History: Effective November 1, 1992.

General Authority: NDCC 57-38-56

Law Implemented: NDCC 57-38-42